Let’s talk: governance
Navigating the company-investor engagement landscape
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By now most large companies have participated in some degree of engagement with institutional investors on corporate governance topics — and in a growing number of instances directors have participated in that dialogue.

These interactions, initially driven by mandatory say-on-pay (SOP) proposals and increasingly expanding to cover other topics, defined the last two proxy seasons. In 2013, a majority of Fortune 100 companies disclosed in their proxy statements that they reached out to investors in connection with their SOP votes, an increase of nearly 50% over the prior year. Company-shareholder engagement will continue to be a primary theme in 2014, one that is likely to be of interest to corporate boards.

In late 2013, EY’s corporate governance team connected with nearly 40 institutional investors, investor associations and advisors to learn about their governance priorities. What we learned may help companies and their board members better understand what’s on the mind of investors and prepare for engagement to make those interactions more productive.

Why engage?

Engagement can be a strategic opportunity. A commitment to ongoing dialogue with investors on corporate governance topics may help companies to:

- **Secure investor support** — some investors are using a company’s engagement practices as an indicator of effective governance. A company’s willingness to engage and listen can enhance investor confidence in the board’s performance. A constructive relationship with long-term institutional investors can result in allies when a company faces strategic challenges or reputational risk.

- **Mitigate potential exposure to activism** — shareholders participating in ongoing conversations with a company are less likely to escalate their concerns publicly. At the same time, these relationships may help a company defend against short-term activist investors.

- **Counter check-the-box proxy voting** — investor outreach, enhanced proxy statement disclosures and responsiveness to investor feedback may offset proxy advisory firms’ views and boost support for management proposals. Engagement may also lead to the withdrawal of shareholder proposals.

- **Identify emerging opportunities** — learning about shareholder concerns as they arise can provide a company with an early indication of what may become broader emerging challenges. This may offer an opportunity for the company to proactively take the lead.

Director involvement in engagement with shareholders

Although most engagement with shareholders includes directors at least occasionally, investors would like to see directors available for engagement more often.

How often do directors engage with shareholders?

- 9% Often
- 20% Never
- 71% Occasionally

How often would investors like directors to engage with shareholders?

- 34% Often
- 66% Occasionally
- 0% Never
The investors we talked with shared their first-hand experiences on corporate practices. Key takeaways to more successful engagement include:

**Investors are not one-size-fits-all**

Investors may share some corporate governance goals — and may even work together to achieve them — but their specific priorities, asks of companies and approach to engagement often vary significantly. The largest asset managers may only engage selectively and from behind closed doors, while some smaller investors may be more inclined to use high-profile public campaigns. Company representatives are not expected to be experts on each investor, but discussions are more productive when there is a basic understanding of investor priorities.

**The heart of engagement is listening and relationship-building**

A critical component of engagement is providing institutional investors with confidence that their voices are being heard and their views are being communicated to the board. A company’s responsiveness, messaging and tone can be as important as the topic of discussion. Most investors prefer to have a dialogue, find common ground, and reach agreement — even if their specific ask is not agreed to by the company. Some investors still feel they need to use the shareholder proposal mechanism to get board-level attention and as an invitation for discussion.

Avoid “engagement for engagement’s sake” … but know when to engage

An introduction to establish a channel for communication can be significant. However, a meeting is not always necessary — an introductory phone call or email can be sufficient. Like companies, investors face resource constraints. Given the extensive holdings of many institutional investors often the best time to lay the groundwork for engagement is outside of “proxy season” — more than 80% of companies hold annual meetings from March to June. Bottom line, don’t wait until there is an issue before initiating investor outreach — develop these relationships outside of season so you can call on them if necessary.

**Preparation is critical to success — a little homework goes a long way**

Agreeing to an agenda beforehand helps to set expectations for meeting outcomes, and ensures that both sides include the right people. It is helpful for companies to meet the individuals who are responsible for proxy voting decisions (portfolio managers may or may not be involved). Although board level involvement is not always needed for engagement to succeed, directors should be involved in certain situations, such as when there is a crisis or when directors have direct oversight of the topic in question. Also, all involved — including executives and directors — should be fully prepared, knowledgeable about the topic under discussion, and active participants. Remember, investors are increasingly using a company’s willingness to engage as a gauge of the effectiveness of a board and company executives.

Focus on company-specific decisions and look past the views of proxy advisory firms

In direct company-shareholder conversations, avoid complaints about proxy advisory firm views and recommendations. Most large investors have their own corporate governance policies and tend to be sensitive to assumptions that, as a group, they blindly follow the vote recommendations of proxy advisory firms. Instead, demonstrate knowledge of why company-specific governance practices are appropriate taking into account broader trends and peer practices. And make the best use of your engagement opportunity by focusing on what investors want to know and demonstrating appropriate board-level attention to these topics.

Institutional investors increasingly expect access to directors for substantive dialogue on corporate governance topics. We believe it should be on every board’s agenda to consider strategies for communicating with investors, including when directors should be involved in that engagement. In this evolving governance landscape, maintaining constructive ongoing relationships with shareholders has more payoff potential than ever.

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**Questions for the board to consider:**

- Has the board developed a strategy for engaging with shareholders on corporate governance topics?
- Is there a process in place to handle requests from shareholders for dialogue and are these requests shared with the board?
- Does the board understand the governance priorities of the company’s largest and most vocal shareholders?
- Has the board identified directors who could speak with investors?
Let's continue the conversation.

Find out more at ey.com/governance or contact one of the following professionals:

**Allie Rutherford**  
Center for Board Matters  
Ernst & Young LLP  
+1 202 327 7026  
allie.rutherford@ey.com

**Ruby Sharma**  
Center for Board Matters  
Ernst & Young LLP  
+1 212 773 0078  
ruby.sharma@ey.com